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MEMORANDUM FOR: THE RECORD

DDI- 5451/82

Briefing notes drafted by SOVA and OGI in response to DCI request.

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Chief
Soviet Economy Division
Office of Soviet Analysis

Date 30 June 1982

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30 June 1982

Soviet Grain Prospects and the US-Soviet Long-Term Grain Agreement

A Cabinet Affairs Staffing Memorandum proposes four options regarding the US-USSR Grain Agreement, which will expire on 30 September 1982.

- o Allow the agreement to expire on 30 September 1982.
- o Extend the agreement for one year.
- o Extend the agreement for two or more years while amending it to provide higher minimum purchase requirements.
- o Negotiate a totally new US-USSR grain agreement.

Crop Prospects and Import Requirements

Poor weather in recent weeks has all but ruined chances for a good Soviet grain harvest in 1982.

- o Soviet planners had called for a 238-million-ton grain crop, but the best crop possible appears to be about 185 million tons.
- o The harvest could be much worse; if the hot, dry weather in the Soviet spring grain area persists, a crop near the size of last year's reported 158-million-ton harvest might be possible.

To save its livestock program and rebuild badly depleted grain stocks, Moscow will need to import as much grain as possible. Imports, however, will be limited by the amount its ports and rail system can handle, about 50 million tons. With a 185-million-ton grain crop and imports of 50 million tons, we estimate that the USSR would be able to again muddle through.

- o Distress slaughtering could be avoided.
- o Meat production could increase marginally above the 1981 reported level of 15.2 million tons.
- o The Soviets would have to purchase about 1 million tons of meat in the world market, as they did in 1981, to maintain per capita meat consumption.

On the down side, if the crop were worse--say 160 million tons--the Soviets would face a critical feed shortage.

- o Some distress slaughtering, primarily of hogs, would be likely.

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- o Even with the additional meat available because of the unplanned slaughtering, meat production probably would still fall below 15 million tons.
- o Record meat imports (1 million tons) would not prevent per capita meat consumption from dropping by about 3 percent during the coming year.
- o Moreover, distress slaughtering would mark a substantial setback for the livestock sector and would depress meat production at least for the next few years.

<u>Sources of Grain Imports</u>

To meet its import requirements, under normal market conditions the USSR will rely on the major grain exporters.

- o Moscow may have already lined up 17 million tons under long term agreements and other purchases from Canada, Argentina, Eastern Europe, Thailand, and Brazil.
- o Depending on the size of this year's crops, non-US grain exporters probably will provide an additional 15 million tons.
- o To acquire much more than 32 million tons while obtaining the mix of feedgrains that it desires, the USSR would probably seek to buy US grain, especially corn. Moscow would like to have more corn because it is on average the most efficient and most economical complement for domestically-produced feedgrains.
- o Although grain prices have fallen somewhat recently, imports of 50 million tons would cost $6 to $6.5 billion.

Should US grain be denied, Moscow could still satisfy much--and perhaps all--of its overall import requirements from non-US suppliers. To do so, however, the USSR would have to be willing to substitute wheat for much of the feedgrain it needs.

- o The major exporters will likely have some 10 to 11 million tons of uncommitted grain (mainly wheat) available.
- o Another 5 to 7 million tons would be available if the Soviets aggressively tapped smaller suppliers and were willing to pay premiums to divert grain from traditional channels.
- o Even with such premiums, the Soviet grain bill for marketing year 1983 would not much exceed $7 billion.

The probable net effect of a US embargo in marketing year 1983 would be a decline in US grain exports.

- o In contrast to the last embargo, opportunities for the US to offset reduced Soviet purchases by penetrating other exporters' markets are limited. Non-Soviet import demand is expected to be stagnant, and the world's exportable supplies of grain are greater than last year.

- o The initial impact of an embargo would be an increase in US stocks of grain, particularly coarse grains.

Paying for Imports

The USSR will have a problem paying for its purchases.

- o Prices for oil and gold--two major hard currency earners--will probably remain weak throughout 1982.

- o Consequently, Moscow will probably continue to rely on short term credits. Soviet traders are presently seeking new, longer-term credits with 270- to 360-day maturities and are attempting to roll over previously acquired credits now coming due.

- o In addition, Moscow will probably again have to reduce imports of non-agricultural commodities, which fell by about 10 percent last year.

Western suppliers could help ease the USSR's financial burden.

- o Moscow might defer almost $4 billion in hard currency payments that would otherwise come due during 1982-84 if it were able to obtain liberal three-year financing from the US and other suppliers rather than the terms that are likely to be available.

- o The USG would probably have to provide US bankers with some guarantees and interest rate subsidies to elicit the more liberal terms. Other major exporters would have to follow suit or see their market shares erode.

- o In the process, the US might well expand its share of Soviet imports.

At the other extreme, the United States could even more actively than at present discourage foreign governments from offering any form of credits through official channels.

- o If the US could convince other governments not to underwrite Soviet grain purchases, Moscow would have to rely solely on commercial financial institutions for grain credits.

- o In these circumstances bankers, who take their cue from government policy, would be reluctant to extend such credits and would demand high interest rates--at least some percentage points over the London Inter-Bank Offered Rate (LIBOR) which is currently around 15 percent. Bankers would also not be likely to offer maturities much in excess of six months.

- o As a result, the costs to the Soviets of their grain purchases would be increased by almost $2 billion compared with outlays under market-determined conditions.

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The LTA Options

The existing LTA provides advantages to both Washington and Moscow.

- For the US, the agreement guarantees sales of 6-8 million tons of US grain regardless of Soviet demand; it offers US farmers the prospect of substantially greater sales in time of relatively low Soviet demand. (In 1977, for example, 6 million tons of the 10.5 million tons the USSR imported came from the US.) Finally, by providing the prospect of a more stable and assured foreign market it eliminates some of the uncertainty of domestic production decisions.

- For the USSR, the agreement continues to provide access to the world's largest and most stable grain producer and the exporter best able to meet Soviet needs for feedgrains. Even so, the USSR continues to consider the US as a market of last resort, preferring to buy the bulk of its grain from other major exporters.

Moscow will not be able to raise grain production rapidly enough in the 1980s to avoid continuing large imports.

- With average weather--and assuming no technological breakthroughs--grain production through the mid-1980s is likely to average only about 215 million tons.

- An average crop of this size would fall at least 30 million tons below the total needed each year to sustain Soviet meat and livestock programs.

Soviet purchases from the US will likely continue even if the LTA lapses.

- Moreover, by allowing the agreement to lapse, the US would be giving additional notice to the USSR that US-Soviet relations cannot be business-as-usual until progress is made on Afghanistan and Poland.

- Without an agreement and in the absence of an embargo, however, the USG would be uninvolved in determining the amount of US grain the Soviets purchased each year.

A new LTA or an extension would offer the opportunity to increase the minimum purchase level and maintain or even increase the US share of Soviet grain purchases.

- The USSR also has an incentive to raise the upper limit above 8 million tons while pushing for guaranteed delivery of purchased grain. The United States, being the largest and most consistent world grain exporter, could provide the USSR with a cushion against the volatility of production in other grain exporting countries.

- It would also consider our willingness to negotiate a new agreement as a move toward business-as-usual in commercial relations.

- But Western Europe and Japan would find the continuation of sanctions on energy equipment combined with US-Soviet negotiations on a new LTA incongruous.

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